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IN THE

Supreme Court of the United States

October Term, 1979
No. 78-1577

SEARS, ROEBUCK AND CO.,

Petitioner,

vs.

COUNTY OF LOS ANGELES and CITY OF COMPTON,

Respondents.

On Petition for a Writ of Certiorari to the Court of Appeal of the State of California, Second Appellate District.

Motion for Leave to File Brief Amicus Curiae in Support of Petitioner and Brief of Charles R. Ajalat as Amicus Curiae in Support of Petitioner.

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Motion for Leave to File Brief Amicus Curiae in Support of Petitioner.

Charles R. Ajalat, Ajalat & Polley, hereby respectfully moves for leave to file the attached brief amicus curiae in this case. The consent of the Attorney for the County of Los Angeles has been obtained. The consent of the Attorney for the Petitioner was requested and refused.

Charles R. Ajalat, Ajalat & Polley represents, in pending litigation, clients who have been denied the benefits of the statute whose constitutionality has been questioned. In addition to being an active practitioner in the state and local tax area, he teaches state and local taxation in the Masters of Taxation program

at the University of Southern California. He was involved in the passage of the statute here involved as well as all of the other California developments related to and leading up to *Michelin Tire Corp. v. Wages* (1976) 423 U.S. 276, 46 L.Ed.2d 495, 96 S.Ct. 535. For each of these reasons, he has an interest in the case at bar and the development of the law in this area.

Based on relatively extensive oral discussions with both parties, it is believed that the parties will not or have not sufficiently recognized the extent to which this case is an integral part of the important line of state tax cases decided by this Court since 1976 and its interrelationship with that line of cases. This case, too, involves the problem of the effect on interstate or foreign commerce of a state or local government decision to tax, or (as in this case) not to tax. Further, based on those discussions, it is believed that the parties will not or have not sufficiently set forth the purpose and effect of the statute whose constitutionality is questioned. Both of these considerations are relevant to a proper disposition of the case and to the development of federal constitutional law as it impacts on state and local taxation.

Charles R. Ajalat, Ajalat & Polley, therefore, urges that leave be granted to file a brief as amicus curiae and respectfully so moves the Court.

Respectfully submitted,

CHARLES R. AJALAT,
AJALAT & POLLEY,
Amicus Curiae.

BRIEF OF AMICUS CURIAE ON THE MERITS IN SUPPORT OF PETITIONER.

I.
INTEREST OF AMICUS CURIAE.

Amicus Curiae represents, in pending litigation, clients who have been denied the benefits of the statute whose constitutionality has been questioned. In addition to being an active practitioner in the state and local tax area, Amicus Curiae teaches state and local taxation in the Masters of Taxation program at the University of Southern California. Amicus Curiae was involved in the passage of the statute here involved as well as all of the other California developments related to and leading up to *Michelin Tire Corp. v. Wages* (1976) 423 U.S. 276, 46 L.Ed.2d 495, 96 S.Ct. 535. For each of these reasons, Amicus Curiae has an interest in the case at bar and the development of the law in this area.

II.
ARGUMENT.

This case is an integral part of the important line of state tax cases decided by this Court since 1976. It, too, involves the problem of the effect on interstate or foreign commerce of a state or local government decision to tax, or (as in this case) not to tax.

A. Michelin, Complete Auto, Japan Lines and the Case at Bar Should Establish a Coherent Interstate-Foreign Commerce Dichotomy.

In the last three years, this Court in an exciting and direct way has come to grips with the age old problems presented by state taxation which are at the same time some of the most difficult and some of the most important ones of our constitutional

framework. The Court is recognizing that the constitutional concepts cut across all the state tax lines and it is making a coherent, workable conceptual framework out of what has otherwise been chaos.

Nexus and apportionment in relation to benefit—the two key *due process* considerations—have long ago been set forth by this Court with recent affirmation: Nexus, having been broadly defined, is often no longer an issue (*but see National Geographic Society v. California Board of Equalization* (1977) 430 U.S. 551, 51 L.Ed.2d 631, 97 S.Ct. 1386); apportionment, although it still presents extremely difficult issues, especially in the income tax area (see *Moorman Manufacturing Co. v. Bair* (1978) 437 U.S. 267, 57 L.Ed. 2d 197, 98 S.Ct. 2340), has been deemed by the courts often to be best handled by the legislature.

Commerce Clause problems, on the other hand, have evolved somewhat more slowly in terms of solutions based on consistent, practical theories. Not until recently has the Court been able to come to grips with the application of state taxes to interstate commerce and foreign commerce other than to recognize that states could not discriminate against such commerce (recently reaffirmed in *Boston Stock Exchange v. State Tax Comm'n* (1977) 429 U.S. 318, 50 L.Ed.2d 514, 97 S.Ct. 599, and *Michelin Tire Corp. v. Wages, supra*).

The Court's first step toward making sense out of nondiscriminatory apportioned state taxation as it relates to interstate commerce and foreign commerce was the dramatic elimination of the Import-Export Clause as a separate consideration. (*Michelin Tire Corp. v. Wages, supra.*)

The Court then dealt with *interstate commerce* in terms of the modern realities and our strong federal

system and made the income tax rules conform, as they should, to the theory behind the property tax rules: Nondiscriminatory, properly apportioned taxes can be applied to all commerce between the states, including transactions exclusively in interstate commerce. (*Complete Auto Transit, Inc. v. Brady* (1977) 430 U.S. 274, 51 L.Ed.2d 326, 97 S.Ct. 1976.)

Finally, the Court turned its attention to the key problem of state taxation today—the effect of state and local taxes upon the relations of the sovereign federal government with other sovereign governments. Refusing to use the outdated and inconsistent "home port doctrine," the Court dealt with the key issue itself—the effect of state taxation upon *foreign commerce* and held that "When construing Congress' power to 'regulate Commerce with foreign Nations,' a more extensive constitutional inquiry is required." (*Japan Line, Ltd. v. County of Los Angeles* (1979) ..... U.S. ....., 60 L.Ed.2d 336, at 346, 99 S.Ct. .....)

The Court is now faced with clarifying the coherent structure it has erected in *Complete Auto* (interstate commerce) and *Japan Line* (foreign commerce). The vehicles before the Court are the case at bar and the pending cases of *Mobil Oil Corp. v. Vermont Com'r of Taxes* (No. 78-1201) and *Asarco Inc. v. Idaho State Tax Comm.* (No. 78-1839).[1] Unless the

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[1]The issues presented in this brief may not affect the pending *Mobil Oil* and *Asarco* cases, *supra,* unless the Court applies the "forbidden effect" test of *Complete Auto Transit, Inc. v. Brady, supra,* 51 L.Ed.2d at 337, or unless it overturns (as many have argued it should) the doctrine of *Flint v. Stone Tracy Co.* (1911) 220 U.S. 107, 55 L.Ed. 389, 31 S.Ct. 342. (See *Pacific Co. Ltd. v. Johnson* (1932) 285 U.S. 480, 76 L.Ed. 893, 52 S.Ct. 424), suggested by some to be the key remaining outdated anachronism in the state tax area after the elimination of the "original package" and "home port" doctrines.

Court is to go back to additional legal fictions and artificial distinctions, it must use the current term's cases to make clear that foreign commerce itself must have absolute immunity from state *taxation* under the foreign commerce clause,[2] and that state statutes furthering that goal, as in the present case, are valid and desirable.

Legal fictions and artificial distinctions, if they are adopted, will not only cause years of litigation and burdens on the courts, but will ultimately have to be swept away as were the original package doctrine in *Michelin,* the franchise tax-income tax distinction in *Complete Auto,* and the home port doctrine in *Japan Line.* The alternative is workable and consistent with the federal constitution prohibition of discrimination *against* foreign commerce. The alternative is to allow nondiscriminatory, properly apportioned state taxation of interstate commerce; to prohibit any state taxation of foreign commerce; and to allow states, consistent with the policies behind such prohibition, to favor foreign transactions over local and interstate ones, subject to the ultimate responsibility they owe in this regard to their electorates and the Congress.

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[2]For example, the *Japan Line* rule should not be limited solely to foreign based instrumentalities exclusively engaged in foreign commerce but should be applied to domestic based instrumentalities to the extent they are engaged in foreign commerce. Any reference to prohibiting taxation of foreign commerce, of course, would mean no expansion of the rules applicable where such foreign commerce has terminated. For example, foreign goods which are not in transit have no *constitutional* immunity. *Michelin Tire Corp. v. Wages, supra.*

B. Japan Line's Special Treatment of Foreign Commerce Applies to the Case at Bar.

Japan Line, Ltd. v. County of Los Angeles, supra, prohibited the taxing authority from taxing foreign based instrumentalities of commerce engaged exclusively in foreign commerce. This Court, noting that the argument was "not without weight," recognized appellee's concern that "by exempting appellant's containers from tax, the state in effect will be forced to discriminate against domestic, in favor of foreign commerce."

The case at bar is not one wherein the constitution *requires* a similar discrimination against domestic in favor of foreign commerce. Rather, the issue is whether the state legislative action must be upheld as properly consonant with the special place and protection from state *taxation* given foreign commerce by the federal government. Although *Japan Line* does not constitutionally require the result, the policies behind *Japan Line* require a holding that the statute is valid.

The proper analysis starts by recognizing that the *Japan Line* rationale must apply to foreign commerce generally and not to a particular aspect of such commerce. To avoid inconsistency and artificiality, the special treatment of foreign commerce granted in *Japan Line* cannot and must not be limited to instrumentalities of foreign commerce. Further, it must not be limited to foreign based domiciliaries, nor limited to exclusively foreign commerce (as opposed to the portion of a business which is in foreign commerce)

To limit *Japan Line* to instrumentalities of foreign commerce would be to say the vehicle that carries the commerce is more important than the commerce itself.[3] To limit the constitutional protection of foreign commerce to foreign based companies would be to create a non-intended constitutional discrimination against American based companies doing business in foreign commerce.

To hold that foreign commerce is special if it is engaged in exclusively, but when interstate commerce is also engaged in the constitutional immunity is lost, would be irrational.

The enhanced risk of multiple taxation test set forth in *Japan Line* applies whenever any aspect of foreign commerce is involved, especially in today's narrowing and interdependent world. "[N]either this Court nor this Nation can ensure full apportionment when one of the taxing entities is a foreign sovereign." (*Japan Line, Ltd. v. County of Los Angeles, supra,* 60 L.Ed. 2d at 247.) If *foreign commerce* is involved and California can *tax* any aspect of it, it follows that foreign sovereigns would also have a theoretical basis to tax and its apportionment formula is not under the control of this Court or this Nation.

Japan Line also teaches that it must be inquired whether the *tax* prevents the Federal Government from "speaking with one voice when regulating commercial relations with foreign governments." (*Japan Line, Ltd. v. County of Los Angeles, supra,* 60 L.Ed.2d at 349.)

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[3]Compare *Japan Line, Ltd. v. County of Los Angeles, supra,* 60 L.Ed.2d at 349, fn. 14, "In Washington Revenue Dept., the Court, holding that the state tax at issue did not prevent 'speaking with one voice,' noted: 'No foreign *business* or vessel is taxed.' " (emphasis added).

The rationale for the inquiry is to prevent international disputes over reconciling apportionment formula and retaliation against the taxing state and other states of the United States.

As the Solicitor General in this case has said: "In sum, the decisions of this Court involving imports, exports, and foreign commerce uniformly emphasize that one of the principal purposes of the Constitution was to assure that the States did not impede or obstruct importation, exportation, or foreign commerce." (Brief of the United States as Amicus Curiae, p. 9.)

These policies apply to all aspects of foreign commerce and cannot be limited to instrumentalities that are foreign-owned and exclusively in foreign commerce. To not accept this principle will cause litigation, inconsistencies and impossible lines to draw for years to come.

If *Japan Line,* then, prohibits state taxation of foreign commerce because of the inability to control foreign taxation and the fact that state taxation can cause international disputes and retaliation, what does this teach us about state exemption of goods being transshipped through California which have a foreign source or foreign destination? Such state exemption does not involve the difficult problem of this Court or this Nation telling foreign sovereigns what to do. Such state exemption lessens rather than heightens the likelihood of international disputes and retaliation. Although an exemption of foreign commerce from certain countries would be prohibited, exemption of all foreign source or foreign destination transshipments is not only a valid state legislative power but one consonant with the foreign commerce policies behind the Commerce

Clause. Such a statute should be encouraged and not prohibited. California Revenue and Taxation Code Section 225 which lessens burdens on foreign source or foreign destination transshipments must be upheld as proper legislative action consonant with the special place and protection from state taxation given foreign commerce by the federal government.

C. The Statute Permissibly Discriminates in Favor of Foreign Transactions and Is Consistent With the Free Flow of Goods Between Sovereign Nations.

1. Boston Stock Exchange.

The California Court of Appeal held, based on *Boston Stock Exchange v. State Tax Comm'n, supra,* that Revenue and Taxation Code Section 225 unconstitutionally discriminated in favor of foreign commerce and against domestic commerce. We must recall again that the result of *Japan Line* appears to require "the state in effect . . . to discriminate against domestic in favor of foreign commerce." (See page 7 above.) Although there is no constitutional requirement of discrimination in the case at bar, as set forth above, the policies of *Japan Line* make clear that such a discrimination is not unconstitutional.

The *Boston Stock Exchange* case is not relevant to the case at bar because it was in the interstate context. It prohibited "a direct commercial advantage to local business" by reason of taxing "laws that favor local enterprises at the expense of out-of-state businesses." (429 U.S. at 329.) The discrimination "between two types of interstate transactions in order to favor local commercial interests over out-of-state businesses" (*Id.* at 335(was prohibited because it went against the

policy of creating "an area of free trade among the several States." (*Id.* at 328.)

Where foreign transactions are involved, different considerations are at issue. As the Solicitor General made clear, there is no constitutional prohibition against favoring imports and exports over domestic goods. In fact, the Import-Export Clause makes such a differentiation, and does so as a matter of absolute prohibition against certain state taxes on imports or exports. The purpose of the Import-Export Clause—to assure a free flow of goods between sovereign nations and the inland states of this country—is precisely furthered by Revenue and Taxation Code Section 225.

This Court has never held that there could not be discriminations in *favor* of foreign commerce, but rather only prohibited discriminations against foreign commerce.

> "[T]he decisions of this Court involving imports, exports and foreign commerce uniformly emphasize that one of the principal purposes of the Constitution was to assure that the states did not impede or obstruct importation, exportation or foreign commerce. . . . [The statute] facilitates importation and exportation and assures that imports and exports passing through the state will not be impeded even to the extent of the impact of a generally applicable property tax. While such action may not be constitutionally required, it is not, as the decision below erroneously held, constitutionally prohibited. Nothing in the Commerce Clause prevents a state from favoring imports and exports beyond the extent required by the Import-Export Clause." (Brief for the United States as Amicus Curiae, pp. 9-10.)

2. Tariffs.

The Court of Appeal in the case at bar also held that the federal tariff power was undermined by the statute. As noted by the Solicitor General, the reasoning of *Michelin Tire Corp. v. Wages, supra,* holds this irrelevant. (423 U.S. at 287.) More importantly, it should be clear that state and local taxes do not impact tariff decisions inasmuch as it would be impossible administratively for the federal government to take into account all state and local taxation or non-taxation in determining tariff policy. To look at the thousands of cities, counties, states and special districts and the impact on foreign goods of nondiscriminatory, apportioned taxes where there was nexus in relationship to benefit; and then to determine the impact of nondiscriminatory decisions by other such entities not to tax; and then to keep track of all changes in the taxing policies of these thousands of entities, would be undesirable even if possible. Further, the statute in question clearly applies to imports and exports in the transportation stream from all countries and does not discriminate in favor of or against any nation.

3. Free Trade.

Of greater importance than the inapplicability of *Boston Stock Exchange* or relationship to tariffs is the effect of the statute in relationship to the key federal policy as to foreign commerce: free trade among sovereign nations absent specific Congressional decisions to the contrary.

With the modern interdependence of nations, the problems of balance of payments and the need of nations to encourage foreign purchases of their own goods, there is a strong impetus to make the flow

of goods between sovereign nations and the United States as unencumbered as possible *vis-à-vis the states.*

The statute clearly supports the flow of foreign trade with the United States. To prohibit the state legislature from advancing that trade would hurt the federal policy rather than help it. To not allow the states to take a position consonant with that of the federal government would be detrimental to the federal position. If Congress wished to encourage state furtherance of its policies, it would be required to pass statutes in every conceivable area asking for such aid, and a decision invalidating Revenue and Taxation Code Section 225 would make states wary of whether, notwithstanding general federal approval, this Court might change their statutes.

4. Responsibility to Their Electorates.

It must be noted that the major discrimination under Revenue and Taxation Code Section 225 is that *California* based manufacturers who export goods to foreign countries and import goods to California are not exempt, whereas their counterpart exporters or importers in Arizona are exempt.

In fact, California could not favor both foreign transshipments *and* local origination or destination transactions at the expense of interstate transactions, for the discrimination between the latter two would violate *Boston Stock Exchange.*

Thus, a strong, built-in check on the system exists in that the California legislature is responsible to the California electorate as to any favoring of foreign transshipments over other commerce. This factor would probably not be enough by itself to validate an interstate discrimination. When combined with the special status

of foreign commerce, with which the statute is consonant, however, it makes clearer that not only is free trade between sovereign nations furthered by the statute; but, there are built-in protections to prevent serious discrimination against interstate commerce.

5. Free Flow of Commerce to Inland States.

Rather than impede interstate commerce, it must be emphasized that the purpose of Revenue and Taxation Code Section 225, in consonance with the Import-Export Clause and the regulation of foreign commerce, was precisely to help the free flow of goods from foreign countries to the other states of the United States. Thus, not only is there encouragement of a free flow of goods between nations but between the states themselves.

III.
CONCLUSION.

For all of the foregoing reasons, Amicus Curiae urges this Court to reverse the California Court of Appeal and uphold the constitutionality of Revenue and Taxation Code Section 225.

Respectfully submitted,

CHARLES R. AJALAT,
AJALAT & POLLEY,
Amicus Curiae.